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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington D.C.

FCC 92-257
38415

In the Matter of

Price Cap Performance Review
For AT&T

) CC Docket No. 92-134 ✓
)

NOTICE OF INQUIRY

Adopted: June 18, 1992

; Released: July 17, 1992

Comment Date: August 21, 1992

Reply Comment Date: September 21, 1992

By the Commission:

I. INTRODUCTION

1. With this Notice, we begin the fourth year review of AT&T's performance under price cap regulation. As the Commission stated when it adopted price caps for AT&T in 1989, this review will be a comprehensive examination of the effects of price cap regulation using all available data and information. To begin this inquiry, the Notice summarizes information already collected by the Commission in monitoring the course of AT&T's performance since price cap rates took effect on July 1, 1989, including data on rates, earnings, service quality, and the development of competition in the long distance marketplace. Overall, the data indicate that price cap regulation has worked well, resulting in the lower rates, innovative services, and improved efficiency we sought to achieve. Finally, the Notice establishes a schedule for the submission of additional data, analysis, and comments on AT&T price caps regulation.

II. THE AT&T PRICE CAP PLAN

2. The Commission began development of the AT&T Price Cap Plan in 1987, as part of a fundamental reappraisal of the rate regulation it applies to telecommunications common carriers.¹ The reappraisal was precipitated by the changes that have swept the telecommunications industry in the last few decades, and accelerated since the AT&T Divestiture. Technological advances in computers, fiber optics, microelectronics, and many other areas transformed

¹ Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Notice of Proposed Rulemaking, 2 FCC Rcd 5208 (1987) (Notice); Further Notice of Proposed Rulemaking, 3 FCC Rcd 3195 (1988) (Further Notice); Report and Order and Second Further Notice of Proposed Rulemaking, 4 FCC Rcd 2873 (1989) (AT&T Price Cap Order); modified on recon. 6 FCC Rcd 665 (1990) (AT&T Price Cap Reconsideration Order), appeal docketed AT&T v. FCC, No. 91-1178 (D.C. Cir. April 15, 1991).

the capabilities of "plain old telephone service" while expanding the range and quality of new services. In place of the monolithic Bell System, customers may now select their telecommunications equipment and services from hundreds of suppliers offering an ever-expanding menu of choices.

3. In advancing an AT&T Price Cap Plan, the Commission laid the theoretical and empirical foundation for a regulatory regime that would respond to these dramatic changes.² Traditional "cost-plus" rate of return regulation focuses on establishing a reasonable limit on the carrier's profits. This approach requires both the carrier and the Commission to engage in a demanding range of operations, including the examination of the carrier's costs, the separation of those costs between the federal and state jurisdictions, the determination that those costs are reasonable, the allocation of costs among individual services, and the determination of a reasonable rate of return upon the invested capital. The limitations and drawbacks of such "cost-plus" regulation include distorted incentives in capital investment, encouragement of cost-shifting when the carrier also participates in more competitive markets, and little incentive to introduce new and innovative services.³

4. The Commission has concluded in the past that rate of return regulation does not encourage optimal efficiency. Under traditional rate of return regulation, the carrier's allowed profits are computed from its total invested capital, whether or not the carrier is using capital, labor, operational methods, and pricing in the most efficient manner. To maximize its profits, the company has an incentive to manipulate its inputs of capital and labor, without regard to efficiency, and to adopt strategies for investment and pricing based upon what it expects the regulatory agency might wish, not necessarily what best serves its customers and society.

5. Correcting such unintended results requires elaborate regulatory structures. The direct costs of such regulation for the regulator, the regulated, and the ratepayer are not trivial: the costs of delay and litigation involved in applying these complex structures during periods of rapid change can also be substantial.⁴

² The theoretical and legal bases for the FCC's price cap regulation were outlined by J.R. Haring and E.R. Kwerel, in OPP Working Paper No. 22, "Competition Policy in the Post-Equal Access Market," (February 1987) and K.B. Levitz in OPP Working Paper Series No. 23, "Loosening the Ties That Bind: Regulating the Interstate Telecommunications Market for the 1990s" (February 1987).

³ There is an extensive body of literature examining the effects of rate of return regulation. See, e.g., H. Averch and L. Johnson, "Behavior of the Firm Under Regulatory Constraint," 52 Amer. Econ. Rev. 1052 (1962); 2 A.E. Kahn, The Economics of Regulation, ch. 2 (1971); and K.E. Train, Optimal Regulation, ch. 1 (1991).

⁴ An early version of price caps was developed by the British Government to regulate British Telecommunications Plc (BT), which was privatized fully in 1984. Under this plan, the weighted average price of a basket of services could

6. A price cap plan improves on traditional regulation by creating positive incentives for reasonable rates, innovation, productivity growth, and accurate cost allocation, while reducing regulatory burdens. The plan's method is to control prices directly, rather than indirectly by examining whether levels of expenses, investment, and profits are reasonable.

7. For AT&T, the Commission's price cap plan created three service baskets. The division of the services among baskets was designed to discourage cross-subsidization between the baskets while permitting pricing flexibility for more rational rate structures for the services within each basket. Basket 1 includes residential and small business services like ordinary long distance services and optional calling plans for these services. Basket 2 includes inbound 800 services. Basket 3 includes other price cap services used by businesses, such as private line, private network, and various data transmission services and facilities. The Commission directed that the average price of services in each basket should change annually by no more than the level of inflation in the US economy (as measured by the Gross National Product Price Index or GNP-PI), reduced by an additional productivity factor of 3 percent. This factor represented efficiency growth that the Commission judged was challenging yet achievable, above the 2.5 percent rate of productivity growth achieved historically under rate of return regulation. A Consumer Productivity Dividend (CPD) of 0.5 percent was added to ensure that customers would receive the first benefits of the expected increase of productivity. Under this system, the Commission expected that customers would benefit from this growth in efficiency through lower rates, and in any case would be protected from unreasonable rates.

8. Customers were also protected from large rate shifts by rate bands within the baskets. These bands limit the range within which AT&T may change prices during a year. Typically, the bands limit annual price changes within basket service categories to a range of 5 percent around the change in the overall basket index, with tighter bands for night and weekend rates and the composite residential rate.⁵

9. For its part, AT&T was given the incentive to achieve even higher

rise by no more than the increase in an index of retail prices, reduced by the so-called "X" factor of 3 percent. For example, if inflation was 5 percent, the basket price could rise by no more than 2 percent. See I.M. Stelzer, "Regulating Telecommunications In Britain: A New Alternative of the U.S. Approach," *Telematics*, Vol. 3, No. 9 (September 1986). These price controls were adopted for 5 years. Upon review of the program with BT in 1988, the Director General of the Office of Telecommunications extended the plan for 4 years, with an X factor to 4.5 percent, and modified other provisions. In 1990 the overall X factor was moved to 6.25 percent. OFTEL, *The Regulation of BT's Prices: A Consultative Document*, p. 6 (January 1992). OFTEL has recently proposed a 7.5 percent factor to begin on August 1, 1993. OFTEL Press Notice, June 9, 1992.

⁵ Section 61.47 of the Commission's Rules, 47 C.F.R. Section 61.47.

productivity growth because the Commission simultaneously removed limits upon the carrier's profits. The effect is to simulate incentives similar to those in competitive markets, where higher profits are the rewards for greater efficiency and innovation, while falling profits are the penalty for inefficiency or error. Thus, if AT&T could achieve productivity growth above the 3 percent productivity factor it would be able to retain the higher profits generated by its improved performance. Failure to meet this target would erode earnings, but would not change the schedule of rate reductions for customers. The plan also recognized that some cost changes beyond AT&T's control were not captured by the inflation factor, for example changes in the access rates AT&T pays to local exchange companies. The plan required that these exogenous cost changes be weighted and included in the final formula for computing each basket's caps.

10. The decision to adopt the AT&T price cap plan reflected no conclusions about the state of the interexchange telephone marketplace. The advantages of improved incentives and simplified methods of achieving reasonable rates alone justified these regulatory reforms. The price plans were, however, well suited to be transitional steps to even simpler regulatory frameworks that did recognize the presence and positive effects of competition. Thus, in CC Docket No. 90-132⁶, the Commission concluded that the state of competition in the interexchange marketplace warranted reduced regulation of AT&T's business services. Streamlined regulation was adopted for the Basket 3 services (except for analog private line) and for most services not regulated under price caps.⁷ The Commission also decided that Basket 2's inbound 800 services should become subject to streamlined regulation when the technology for 800 number portability is deployed. Streamlining of Basket 3 services took effect in October, 1991. 800 number portability and streamlining of Basket 2 will occur in the first half of 1993.

11. An integral part of the price cap plan is a periodic review of the results to assure that the plan is functioning as intended. Monitoring and review of AT&T's price cap performance was judged necessary to assure that this regulatory structure functions as intended and in accordance with the Communications Act. The Commission therefore adopted a program combining ongoing monitoring with a formal review of the price cap plan to begin before the end of the third year of price caps, and to be concluded during the fourth year. This review was expected "to consist of a comprehensive examination of

⁶ Competition in the Interstate Interexchange Marketplace, CC Docket No. 90-132, Notice of Proposed Rulemaking, 5 FCC Rcd 2627 (1990), Report and Order, 6 FCC Rcd 5880 (1991) (IXC Rulemaking), modified on recon. 7 FCC Rcd 2677(1992).

⁷ Services excluded from price caps are: special construction services; AT&T's Tariff 11, Tariff 12, and Tariff 16 services; services subject to below-the-line accounting; international private line and record carrier services; contract-based and custom services; certain promotional offerings; and services removed from price caps in the IXC Rulemaking, Docket No. 90-132; and any other services specified by the Commission. Section 61.42(c) of the Commission's Rules, 47 C.F.R. Section 61.42(c).

the effects of price cap regulation, and [would] consider all available measures of market and carrier performance, including, but not limited to, actual prices, achieved rate of return, quality of service, and technological progressiveness."⁸ In evaluating changes to the plan such as the productivity factor, the Commission promised "we will endeavor to ensure that the magnitude of the adjustment does not recreate disincentives to further productivity gains."⁹

12. In this Notice, three years later, we undertake our promised review of the plan's performance and of the need for any adjustments or revisions to the plan. We also present preliminary data gathered during our monitoring of the plan's operation and AT&T's performance. Final data on the first three years of price caps, including final prices, will not be available until after the period closes. We will publish a more complete report of AT&T's performance when those data become available.

III. EXPERIENCE UNDER THE AT&T PRICE CAP PLAN

13. When this Commission adopted price caps in 1989, it was a reshaping of traditional public utility regulation. Now, three years later, price cap and other types of incentive regulation have virtually become the norm.¹⁰ Moreover, the Commission's experience with price caps has been positive. Our experience with the AT&T price cap plan, as described in more detail below, supports the conclusion that price caps appear to have achieved the goals of reasonable rates, effective incentives for efficiency and innovation, and reduced regulatory burdens.

14. The transition from rate of return regulation was accomplished smoothly on July 1, 1989, when AT&T's first price cap tariffs took effect. Customers saw no changes in their services or facilities, but did enjoy significant rate reductions. In the three years since, numerous AT&T tariff filings have been made adjusting rates and introducing services under the simplified, streamlined approach established by the plan, without appearing to compromise the Commission's ability to review these tariffs. AT&T has not sought revision of the plan on grounds that it has been forced into unreasonably low rates, while customers have enjoyed overall rate reductions and a wider choice of service offerings.

⁸ AT&T Price Cap Order, 4 FCC Rcd at 3143.

⁹ Id.

¹⁰ This Commission adopted a modified price cap plan for the interstate services of local exchange telephone companies in 1990 that now covers over 90 percent of interstate traffic and revenues. Public service commissions in 13 states have adopted price cap plans for intrastate long distance services, while most others have either deregulated rates or allowed increased rate flexibility. Few states continue to practice traditional rate of return earnings regulation.

15. These benefits occurred while the national economy was weak. Price caps shifts the focus of ratemaking from the individual carrier's costs to national economic trends and Commission-designated efficiency targets. During the first year of price caps, from July, 1989 through June, 1990, the national economy experienced relatively slow economic growth and moderate inflation. Real Gross Domestic Product (GDP) increased 1.4 percent. The economy moved into recession in the last half of 1990, with falling production of goods and services and increased unemployment. The recession appeared to bottom-out in early 1991, but recovery was sluggish and output remained below mid-1990 levels. Positive signs of slow recovery continued in early 1992. Overall, during the first two and a half years of price caps, national output increased very slightly, an average of 0.3 percent per year. Inflation throughout the period was relatively stable; as measured by Gross National Product Price Index (GNP-PI), prices rose about 10 percent, or about 4.5 percent annually.¹¹

16. Interstate long distance calling was affected by the sluggish economy but stood out as a relatively strong growth sector. Interstate switched access minutes of use grew by 13.3 percent in 1989, 11.1 percent in 1990, and 6.3 percent in 1991. Overall, switched access minutes of use grew from 244.7 billion in 1988 to 327.1 billion in 1991.¹²

A. Prices

17. During the first three years of price caps, AT&T's rates in all three price cap baskets have remained below the price cap limits. Appendix, Chart 1. Because the price cap formula requires that real prices be reduced by 3 percent per year, after adjustment for exogenous cost changes, the plan has achieved its goal of lower rates in real terms. Indeed, despite the economic recession and overall 10 percent increase in general prices during this period, rates for residential customers fell by 4.4 percent. Appendix, Chart 2. Rates also fell substantially in other parts of Basket 1 as well as in Baskets 2 and 3.

18. These lower rates produced substantial consumer benefits. Because AT&T's prices never exceeded the caps, customers received the full amount of the CPD, a consumer benefit totalling \$533 million over the three year period. In fact, AT&T priced below the cap throughout this period, primarily in Baskets 2 and 3; these additional benefits totalled \$668 million. Taken together, the consumer benefits from the CPD and below-cap pricing thus total \$1.2 billion to date. Appendix, Chart 3.

19. AT&T has proposed no above-band rates to date. However, AT&T has made 12 filings proposing below-band rates. The price cap plan permits AT&T to make below-band filings, thus offering even lower rates to customers, but requires that these filings be supported by a showing that the rates recover average variable costs and thus are not likely to be anticompetitive. In one case the

¹¹ U.S. Department of Commerce, Survey of Current Business, March 1992.

¹² FCC Report on Long Distance Market Shares: Fourth Quarter 1991, p. 5, Table 1.

filing was initially rejected for defects in the required cost showing; AT&T corrected its study and the reduced rates were allowed to take effect.¹³ In all other cases, the below-band rates as supported by the average variable cost studies were allowed to take effect without rejection, suspension, or investigation.

B. Earnings

20. AT&T's earnings during this period were somewhat higher on average than in earlier periods. In its annual price caps earnings monitoring reports, AT&T computes returns of 11.0 percent for 1989, 13.7 percent for 1990, and 13.4 percent for 1991. The cumulative interstate rate of return under price caps, from July 1, 1989 through December 31, 1991, was 13.2 percent. Appendix, Chart 4. This compares to the last rate of return prescribed for AT&T of 12.0 percent and the most recent rate of return prescribed for local exchange companies in 1990 of 11.25 percent.

C. Infrastructure

21. Growth in the volume and variety of telecommunications services requires adequate investment to increase and improve telecommunications facilities. In the price cap rulemaking, some commenters expressed concern that AT&T would pursue short-term profits over long-term investment, leading to deterioration of the interexchange network.

22. In fact, AT&T has expanded and modernized its network. According to the blanket facilities authorization AT&T must request annually, its domestic in-service circuits have grown from 1.595 million in 1988, the year before price caps was adopted, to 1.777 in 1990 and a projected 1.812 million in 1992.¹⁴ Appendix, Chart 5. Moreover, AT&T has simultaneously engaged in a rapid technological upgrade of its network, replacing analog and microwave radio facilities with digital and fiber optic circuits. Under price caps, AT&T increased its fiber optic cable mileage by 63 percent, from 704,731 in 1988 to 1,146,924 in 1991. AT&T has also implemented a new dynamic call routing technology that is projected to increase network efficiency.

23. In the facilities review and authorization process, the Common Carrier Bureau has identified several concerns for which additional information is being sought to monitor AT&T's infrastructure. For example, reported in-service facilities initially dropped in 1990, a period when AT&T was converting analog

¹³ AT&T Communications, Revisions to Tariff F.C.C. No. 9, 4 FCC Red 8466 (1989), AT&T Transmittal No. 2043, filed January 18, 1990.

¹⁴ Compare American Telephone and Telegraph Company, File No. W-P-C-6441, Order and Authorization, released July 27, 1990, Appendix B (1990 AT&T Blanket Order) and American Telephone and Telegraph Company, File No. W-P-C-6639, Order and Authorization, released October 23, 1991, Appendix B (1991 AT&T Blanket Authorization), with Application of American Telephone and Telegraph Company, W-P-C-6763, filed December 9, 1991, p. 3.

facilities to digital, before increasing again in 1991.¹⁵ The information obtained by the Bureau should be useful in this proceeding.

D. New Services

24. AT&T introduced 77 new services into the price cap baskets between July 1, 1989 and March 1, 1992. Some of these services bring significant new capabilities to customers using AT&T's network. For example, Dual Party Relay¹⁶ permits hearing and speech-impaired customers who use a Telecommunications Device for the Deaf (TDD) to communicate with hearing persons who do not use a TDD. Its Alternate Number Translation option¹⁷ provides customers with an optional back-up database to improve the reliability 800 and 900 number service calling. More recently, AT&T has proposed a new service that would, for the first time, offer customers a portable long distance number with a package of features for forwarding and routing calls.¹⁸ Other new services present new rate choices for customers, who gain more options in customizing their service programs. For example, a customer may choose to receive rate discounts in return for minimum term and revenue commitments.¹⁹

E. Service Quality and Network Reliability

25. In the AT&T price cap orders, the Commission examined the question of whether price cap regulation might create unintended incentives for AT&T to permit the telephone network to deteriorate. The concern was that AT&T might pursue short term profits at the expense of maintaining facilities and making needed investment. We concluded that this was generally unlikely because of constraints upon AT&T's ability to succeed in such a strategy, including state and federal monitoring, the tariff review and complaint processes, and competition from alternative suppliers of long distance service. We retained existing monitoring programs and reports and directed the Common Carrier Bureau to specify disaggregated reporting requirements to more closely monitor areas where AT&T is subject to less facilities-based competition.²⁰

26. The Commission requires AT&T to file reports semi-annually tracking its performance on service quality indexes measuring the frequency of call blocking. The index was set at 100 for the base period preceding price caps, the first half of 1989. A higher index number indicates a higher percentage of

¹⁵ 1991 AT&T Blanket Authorization, p. 5-7.

¹⁶ Transmittal No. 2763.

¹⁷ Transmittal No. 2640.

¹⁸ EasyReach Service, AT&T Transmittal No. 4041, filed April 28, 1992, effective May 26, 1992.

¹⁹ See, e.g., Transmittal Nos. 2899 and 3031.

²⁰ AT&T Price Cap Order, 4 FCC Rcd at 2951-57.

calls blocked in comparison with the base period. For example, a 10-point increase in this index would mean that an additional 0.1 percent of calls were blocked than in the base period. The figures are reported both for blockage associated with AT&T's network and blockage caused by all factors, including blockage attributable to the facilities of local exchange companies terminating AT&T long distance calls.

27. These reports show blockage slightly above the base period for AT&T's network in all five semi-annual reports, but blockage appears to be declining toward the original levels. Appendix, Chart 6. The highest blockage was in the second half of 1989, which AT&T attributes to the disruptions of Hurricane Hugo in September, 1989 and the earthquake in the San Francisco area in October, 1989.

28. AT&T's network reliability under price caps has also become a matter of growing concern in the past three years, largely because of a series of major service outages on AT&T's network. These included: a software problem in January, 1990 that led to the blocking of more than 60 million call attempts nationwide²¹; a fiber optic cable cut in Newark, New Jersey on January 4, 1991²²; the failure of a central office switch in Manhattan, which blocked over 5 million calls and disrupted air traffic control in much of the Northeastern United States²³; and an outage at a facility in Blackstone, Massachusetts which blocked over 1 million calls and disrupted air traffic control at Boston's Logan Airport.²⁴

29. The Commission has thoroughly investigated each of these outages.²⁵ The causes or set of causes were different in each case. None appeared to be directly traceable to price cap regulation or to any AT&T strategy to maximize short-term profit. The FCC report following each outage recommended specific steps to prevent a recurrence. Nevertheless, the assurance of reliable service to the American public, especially where the public health and safety are at stake, is a matter of the highest priority to this Commission. We have already appointed a blue-ribbon advisory panel, the Network Reliability Council, to examine all issues involving network reliability for the entire telecommunications industry. We expect the Council's investigation and reports

²¹ Report by Chief, Common Carrier Bureau to the Chairman, January 15, 1990.

²² Report by the Common Carrier Bureau on the January 4, 1991 AT&T Northeast Disruption.

²³ Preliminary Report by the Common Carrier Bureau on the September 17, 1991 AT&T NYC Power Outage Network Disruption.

²⁴ Report by the Common Carrier Bureau on the November 5, 1991 AT&T Service Outage at Blackstone, Massachusetts.

²⁵ See fns. 21-24, supra.

will identify cost-effective ways of improving network reliability, such as identifying industry-best practices.

30. The Inquiry we begin today offers a full opportunity for the Commission, assisted by the views of commenters, to consider whether we should take additional steps to assure that AT&T's service quality and network reliability remains at the highest level.

G. The Interexchange Marketplace

31. During the first two and a half years of price caps, AT&T's share of interstate traffic first has declined, although it has recovered a portion of that lost share recently. In the second quarter of 1989, AT&T's last quarter under rate of return regulation, AT&T registered a 64.8 percent share of interstate minutes. Its market share first declined to 62.0 percent in the second quarter of 1990, but has since stayed within a range from 61.8 to 62.8 percent each quarter. FCC Report, Long Distance Market Shares: Fourth Quarter, 1991, released March 24, 1992. See also, Appendix, Charts 7-9.

IV. ISSUES ON WHICH INFORMATION AND COMMENTS ARE REQUESTED

32. As we indicated in the original AT&T price cap order, this review will be comprehensive. Parties should submit all data, information, and analysis relevant to AT&T's performance under price cap regulation. Commenters are of course free to propose any changes they believe will improve the price cap plan. However, we emphasize that the goals of price caps are likely to remain unchanged: greater efficiency and innovation; reasonable rates; state-of-the-art service quality; improvement in consumer welfare; and the minimal regulatory burden required to achieve these other objectives. We do not anticipate reimposing rate of return regulation or making any adjustments to price cap regulation that would reduce the incentives the price cap plan creates. Thus, any proposed modifications should be designed to enhance the plan's ability to achieve the original goals.

33. We also solicit comment on the following issues for inquiry:

Issue 1. Should the AT&T price cap regulations be continued after June, 1993?

Issue background: Our monitoring of AT&T's performance under price caps indicates that the basic structure of the AT&T price cap regulation plan has produced substantial benefits to consumers. We request information and comments on this statement. We also request comments on the schedule for the next comprehensive review.

Issue 2. Should the formulas for computing AT&T's price cap indices be changed?

Issue background: The current formulas for computing the Price Cap Indices use GNP-PI as the measure of inflation, a productivity factor, and adjustments for certain exogenous cost changes. The Actual Price Indexes are computed using the demand in the base year and the change in prices. We request comments and

information addressing changes in these formulas that would better achieve the goals of the price cap plan.

Issue 3: Should the productivity factor used to compute the AT&T price cap indices be changed? In addition or in the alternative, should a one-time change in AT&T's price cap index be required?

Issue background: The present AT&T productivity factor is 3.0 percent per year, including a Consumer Productivity Dividend of 0.5 percent. We request information and comments on whether this factor should be changed. An alternative method of adjusting AT&T's rates in order to increase the benefits to customers would be a one-time adjustment in rates. We request information and comments on whether either or both of these adjustments is warranted.

Issue 4: Should the Commission increase monitoring of AT&T's network reliability and service quality?

Issue background: In addition to monitoring the efforts of the Network Reliability Council, we also are requesting additional information from AT&T regarding its service quality. Commenters are requested to submit data, information, and proposals in this inquiry that in their view will contribute to assuring state-of-the-art reliability and service quality for AT&T.

Issue 5: Should the Commission change AT&T's Basket 1?

Issue background: With the removal of most of Basket 3 and the scheduled removal of Basket 2 from price caps, the price cap plan will apply essentially to Basket 1 residential and small business services. These changes in the operation of the plan, as well as other considerations, might support closer examination of the composition of Basket 1.²⁶

²⁶ One possible area for revision could be the composition of the residential basket. This basket now includes the AT&T ReachOut services, optional long distance calling plans that offer discounts or blocks of calling time in exchange for fixed monthly charges. These plans are designed to attract relatively frequent callers, those for whom the discounts reduce bills more than the monthly charge increases them.

These plans have received a large share of the rate reductions in Basket 1, perhaps because the level of competition and marketing directed at these customers puts more downward pressure on these rates than on the standard long distance schedules for which ReachOut is a substitute. The removal of ReachOut from Basket 1 might well help target productivity gains to the standard schedules, while permitting ReachOut customers to continue to benefit both from competitive choices and the opportunity to use the substitute long distance services that would remain in the Basket.

V. ADDITIONAL INFORMATION

34. The Commission is continuing to monitor AT&T's performance and to gather data, particularly data through the third year of price caps, which ends June 30, 1992. Commenters are requested to assist us by submitting any relevant information they may possess. This information should be as specific and quantitative as possible. General claims without the support of the best available hard data and relevant analysis is likely to receive little weight in this inquiry.

35. AT&T, of course, has unique access to information regarding its interstate operations and facilities. We believe that a comprehensive review of price cap performance, especially as it involves the key issue of whether to modify the current rate levels or productivity factor for the residential and small business services in Basket 1, requires the submission and examination of cost data that demonstrate AT&T's performance in providing those services under price caps. Such data could also help us evaluate a reasonable productivity standard for the future. Aggregate performance measures for all of AT&T's interstate services, including non-price cap services, will not necessarily correspond to the results or prospects for Basket 1 services. Thus, we require AT&T to furnish this additional information as part of our review.

36. Furthermore, given the importance of maintaining and improving network infrastructure, we also direct AT&T to submit additional information regarding its activities and performance in maintaining and improving service quality. This information shall include a complete explanation of factors affecting the service quality index under price caps.

VI. SCHEDULE FOR SUBMISSION OF INFORMATION, COMMENTS, AND REPLIES

37. This review will be conducted as a notice of inquiry proceeding. See 47 C.F.R. Section 1.430. Ex parte comments will be permitted. See 47 C.F.R. Section 1.1204(a)(4).

38. In the past, we have required that parties and commenters submit multiple written copies of their submissions for use by the Commission staff and for inclusion in the public docket file. We believe that submission of data and comments in the form of computer diskettes that can be assembled into data bases would assist both the Commission and the public in evaluating the information submitted in this inquiry. Such a data base would then be available for our use in preparing our report and a separate read-only data base could be made available to members of the public wishing to keep abreast of the record in this proceeding.

39. To create this valuable data base, we request that all commenters submit their comments and submissions of data and information in this proceeding in the form of computer diskettes. These should be IBM PC-compatible, with text files compatible with WordPerfect 5.1 software and spreadsheets compatible with Lotus 1-2-3, the configuration of most Commission PCs. For the purposes of this proceeding commenters should also submit the paper copies required by rule. We will accept comments filed only on paper, but

strongly encourage commenters to also submit their filings on diskettes. We also encourage commenters to comment on and suggest improvements to the procedures we now adopt to create data bases to organize and analyze the information to be gathered in this inquiry.

40. All relevant and timely comments and reply comments will be considered by this Commission. In reaching our decision, this Commission may take into account information and ideas not contained in the comments, provided that such information or a writing containing the nature and source of such information is placed in the public file, and provided that the fact of this Commission's reliance on such information is noted in the Order.

VII. ORDERING CLAUSES

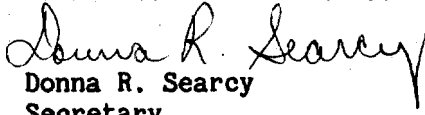
41. Accordingly, IT IS ORDERED that NOTICE IS HEREBY GIVEN OF the inquiry described above and that COMMENT IS SOUGHT on these issues.

42. IT IS FURTHER ORDERED that pursuant to applicable procedures set forth in Sections 1.430, 1.415 and 1.419 of the Commission's Rules, 47 C.F.R. Sections 1.430, 1.415, and 1.419, comments SHALL BE FILED with the Secretary, Federal Communications Commission, Washington, D.C. 20554 on or before August 21, 1992, and reply comments SHALL BE FILED with the Secretary on or before September 21, 1992. To file formally in this proceeding, participants must file an original and four copies of all comments, reply comments, and supporting comments. If participants want each Commissioner to receive a personal copy of their comments, an original plus nine copies must be filed. In addition, parties should file two copies of any such pleading with the Tariff Division, Common Carrier Bureau, Room 518, 1919 M Street, N.W., Washington, D.C. Parties should also file one copy of any documents filed in this docket with this Commission's copy contractor, Downtown Copy Center, 1990 M St. N.W., Room 640, Washington, D.C. 20036. Comments and reply comments will be available for public inspection during regular business hours in the Dockets Reference Room, Room 239, 1919 M Street N.W., Washington, D.C. 20554.

43. IT IS FURTHER ORDERED that AT&T Communications, Inc. SHALL FILE information and data reporting its total revenues, total expenses and taxes, net earnings, rate base, and rate of return for its Basket 1 services for each of the first three years of AT&T price caps and overall, including data showing: the effects associated with changes in depreciation rates granted by the Commission and taking effect within this period; changes in accounting treatment for employee post-retirement benefits; and expenses associated with employee early retirement plans. AT&T is directed to explain each step of how it computes this data and any other data or adjustments it considers relevant to assessing its earnings and performance in providing Basket 1 and other price cap services. AT&T is also directed to submit full information identifying its activities and the factors affecting its service quality under price caps, including all factors affecting its service quality indexes. AT&T is directed to submit this data to the Secretary of the Commission no later than July 31, 1992, in the same manner as other comments in this proceeding.

44. IT IS FURTHER ORDERED that this proceeding will also be a test of methods to improve Commission notice and comment procedures through computer-based filing and docket management approaches. The Commission directs the Chief, Common Carrier Bureau to issue notices and orders necessary to implement this test. We also request the views of interested parties on ways to use computers to improve filing procedures as part of the comment in this proceeding. The Commission strongly urges interested parties to participate in this test.

FEDERAL COMMUNICATIONS COMMISSION


Donna R. Searcy
Secretary

Appendix

Chart 1

AT&T's Price Caps Indices

by Basket and Band
(June 30, 1989 – July 1, 1992)

Index by Basket and Band	June 30, 1989 *	July 1, 1990			July 1, 1991			July 1, 1992 ****		
	Index	Upper Band	Index	Lower Band	Upper Band	Index	Lower Band	Upper Band	Index	Lower Band
Basket 1										
Price Caps Index	96.6	---	94.3	---	---	94.1	---	---	94.3	---
Actual Price Index	98.4	---	94.3	---	---	93.6	---	---	94.3	---
Residential Index	98.8	95.5	94.5	---	95.5	94.1		95.4	94.5	---
Service Band Indices :										
Day	95.7	95.5	91.8	86.3	94.2	89.2	85.2	96.4	91.9	87.2
Evening	99.5	98.8	91.4	90.1	94.5	90.9	86.4	93.3	89.8	85.2
Night/Weekend	99.6	102.4	99.9	93.4	106.3	102.2	97.1	106.1	102.2	97.0
International	99.2	98.3	94.6	88.8	99.4	94.5	89.9	99.3	94.7	89.8
Operator and Card	98.6	100.6	98.7	90.9	103.9	96.4	94.0	104.5	99.6	94.5
Reach Out America	97.1	94.6	88.5	85.5	93.2	88.4	84.4	90.8	86.6	82.1
Basket 2										
Price Caps Index	96.8	---	94.0	---	---	93.8	---	---	94.0	---
Actual Price Index	97.3	---	92.8	---	---	93.4	---	---	93.9	---
Service Band Indices:										
AT&T 800	98.4	98.3	94.7	88.8	100.4	95.3	90.8	96.9	92.5	87.7
Directory 800 **	---	---	---	---	103.3	100.0	95.3	106.5	103.6	98.2
MEGACOM 800	92.3	88.5	85.3	80.0	90.4	85.8	81.8	92.1	87.9	83.4
Other 800	100.0	96.3	90.0	87.0	93.7	89.0	84.8	93.3	89.0	84.4
READYLINE 800	96.5	93.9	90.2	84.8	96.0	91.1	86.8	98.6	94.1	89.2
Former Basket 3 ***										
Price Caps Index	98.3	---	96.7	---	---	97.3	---	---	---	---
Actual Price Index	96.9	---	93.1	---	---	95.9	---	---	---	---
Service Band Indices :										
AT&T WATS	94.8	99.2	94.7	89.8	104.9	99.0	94.9	---	---	---
MEGACOM	92.8	92.9	88.6	84.0	95.7	90.4	86.6	---	---	---
Other Switched	100.2	104.2	99.0	94.3	102.9	97.1	93.1	---	---	---
Other Private Line	99.2	79.8	76.1	72.2	83.1	78.3	75.2	---	---	---
PRO WATS	96.1	95.8	91.1	86.7	98.3	92.8	88.9	---	---	---
SDN	81.9	80.7	76.8	73.0	82.0	77.8	74.2	---	---	---
Voice Grade Private Line	101.2	103.0	98.1	93.2	108.9	102.8	98.5	---	---	---
Restructured Basket 3 ***										
Price Caps Index	---	---	---	---	---	---	---	---	103.2	---
Actual Price Index	---	---	---	---	---	---	---	---	97.9	---

Source: FCC, Common Carrier Bureau, Tariff Division.

* The values of indices on June 30, 1989 are those that immediately preceded price caps regulation: Indices were initiated at 100.0 on December 31, 1988 and price caps regulation began on July 1, 1989.

** The Directory 800 band was added to price caps regulation on July 1, 1991.

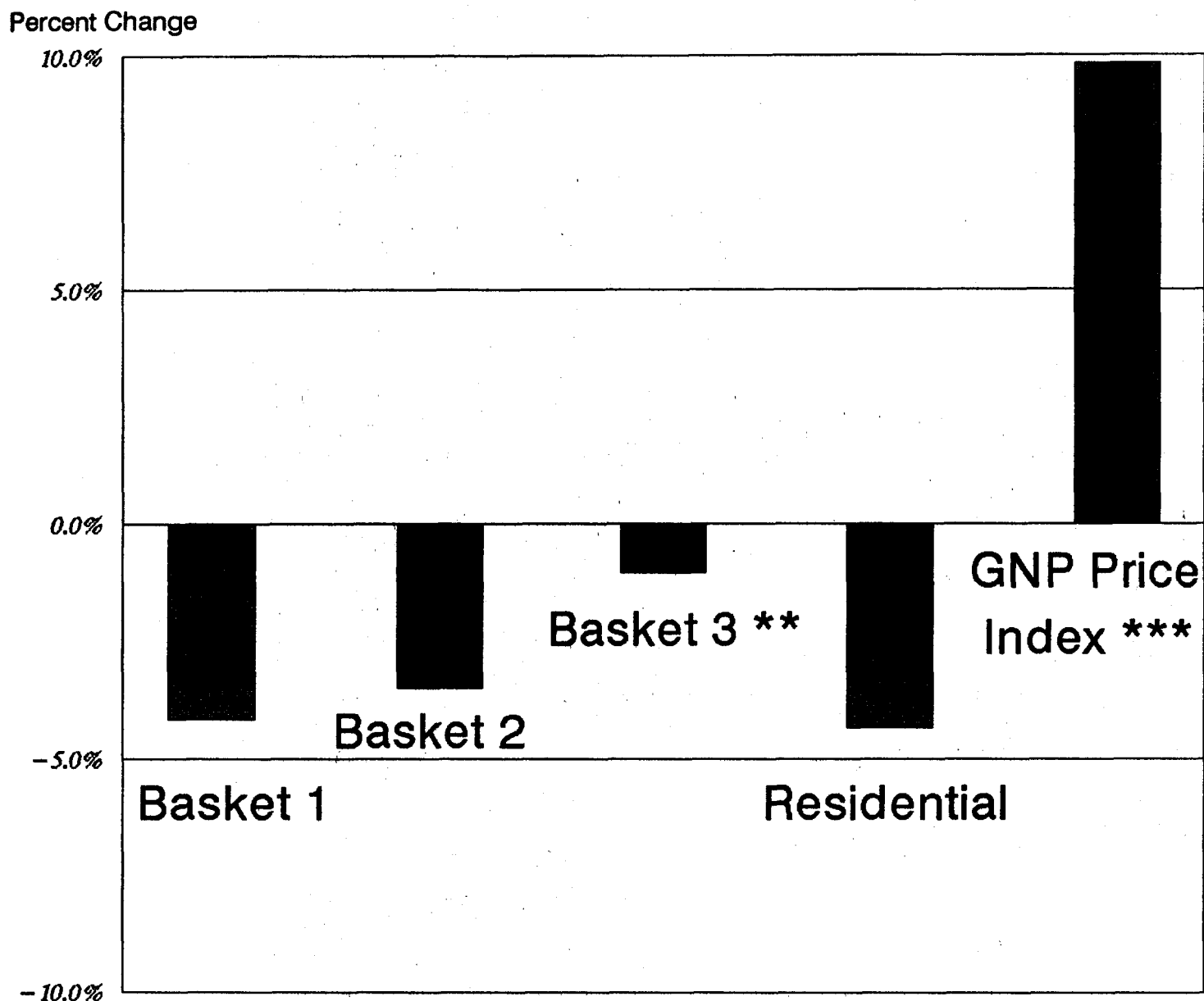
*** Basket 3 indices were reinitiated to 100.0 on August 1, 1991, when Basket 3 was restructured to include only private-line--analog services.

**** July 1, 1992 values are preliminary values from AT&T's annual price cap filing, and are subject to change. These values are based on a May 15, 1992 letter from AT&T to the FCC Secretary, pursuant to Sections 61.41 through 61.49 of the Commission's Rules, 47 C.F.R.

Chart 2

Comparison of Change in AT&T's Price Indices * to Change in GNP Price Index

July 1, 1989 – June 30, 1992



Sources: Chart 1 except for the GNP Price Index (GNP-PI). The GNP-PI is from the Bureau of Economic Analysis, Department of Commerce, Survey of Current Business, various volumes.

* Price indices are the Actual Price Index (API) in each basket and the Basket 1 Residential Index.

** Represents change over two years ending June 30, 1991. An abbreviated period is shown, because most services in Basket 3 were removed from price caps in November 1991.

*** Represents change over two 1/2 years beginning 3rd Quarter 1989 and ending 1st Quarter 1992. An abbreviated period is used, because GNP-PI data is not yet available beyond 1st Quarter 1992.

Chart 3

Consumer Benefits from Below-Caps Pricing and Consumer Dividends

(Millions of Dollars)

Row	Item	1st Price Caps Year	2nd Price Caps Year	3rd Price Caps Year	Total **
1.	Amount by which AT&T has exceeded regulatory requirements by pricing below the cap	\$258	\$205	\$205	\$668
2.	Consumer Productivity Dividend	\$85	\$179	\$269	\$533
3.	TOTAL CONSUMER BENEFIT *	\$343	\$384	\$474	\$1,201

Source: FCC, Common Carrier Bureau, Tariff Division.

* Equals Row 1 plus Row 2.

** Equals the sum of the years.

Notes:

1st Price Caps Year is December 31, 1988 through July 1, 1989.

2nd Price Caps Year is July 2, 1989 through July 1, 1990.

3rd Price Caps Year is July 2, 1990 through July 1, 1991.

Chart 4

AT&T's Interstate Rate of Return

(Thousands of Dollars)

Row	Item	1989	1990	1991
1	Total Revenues	\$25,945,517	\$25,204,356	\$25,672,542
2	Total Expense & Taxes	\$24,719,988	\$23,666,092	\$24,177,121
3	Net Earnings	\$1,225,529	\$1,538,264	\$1,495,420
4	Rate Base (Avg. Net Investment)	\$11,145,915	\$11,207,433	\$11,151,312
5	Rate of Return (Percent)	11.00%	13.73%	13.41%

Source: FCC, Common Carrier Bureau, AT&T's Interstate Rate of Return Report, 1991, 1990, 1989.

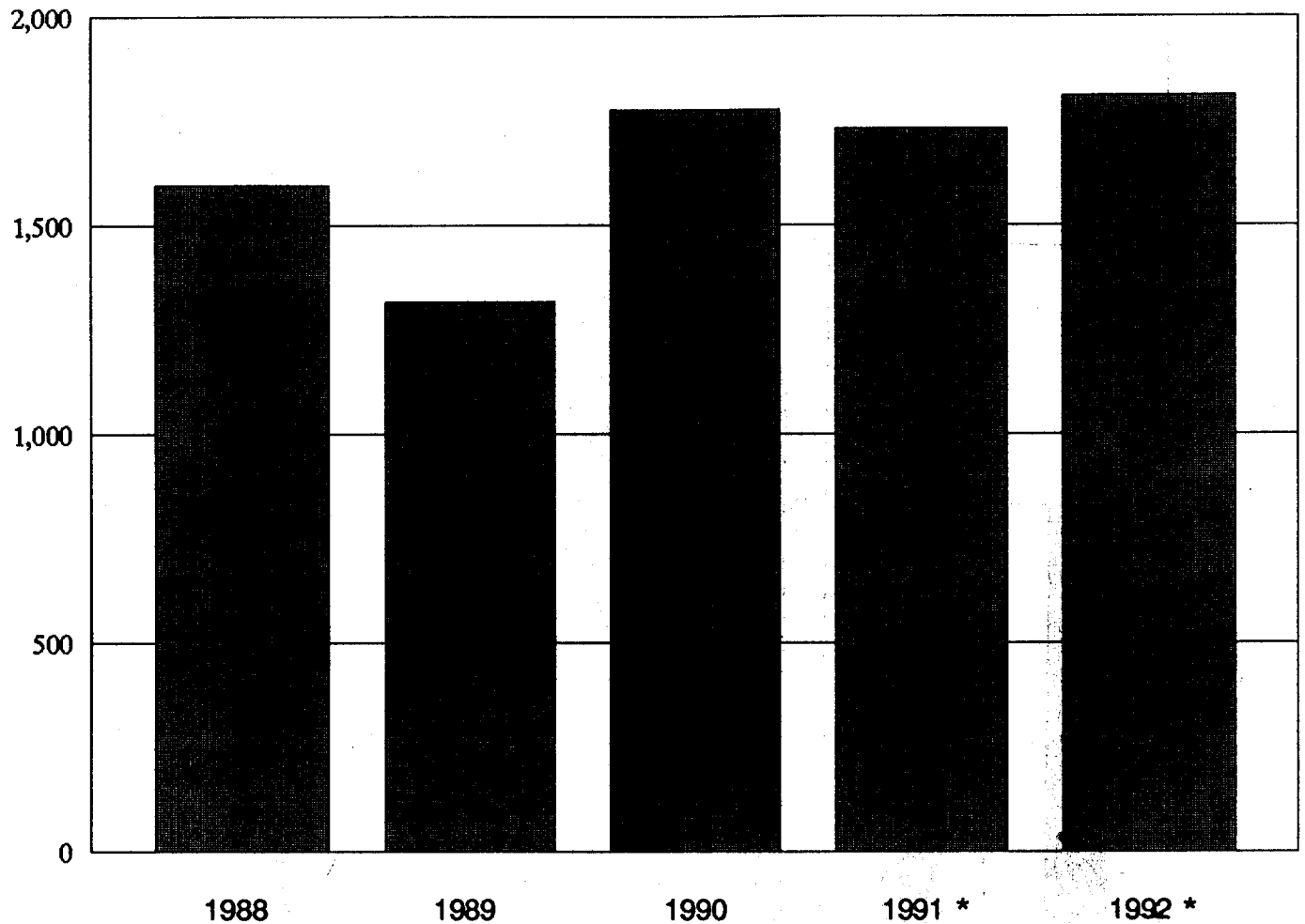
Notes:

Row 3: Row 1 minus Row 2.

Row 5: Row 3 divided by Row 4.

Chart 5

AT&T's Circuit Counts



Source: FCC, Common Carrier Bureau, Domestic Facilities Division.

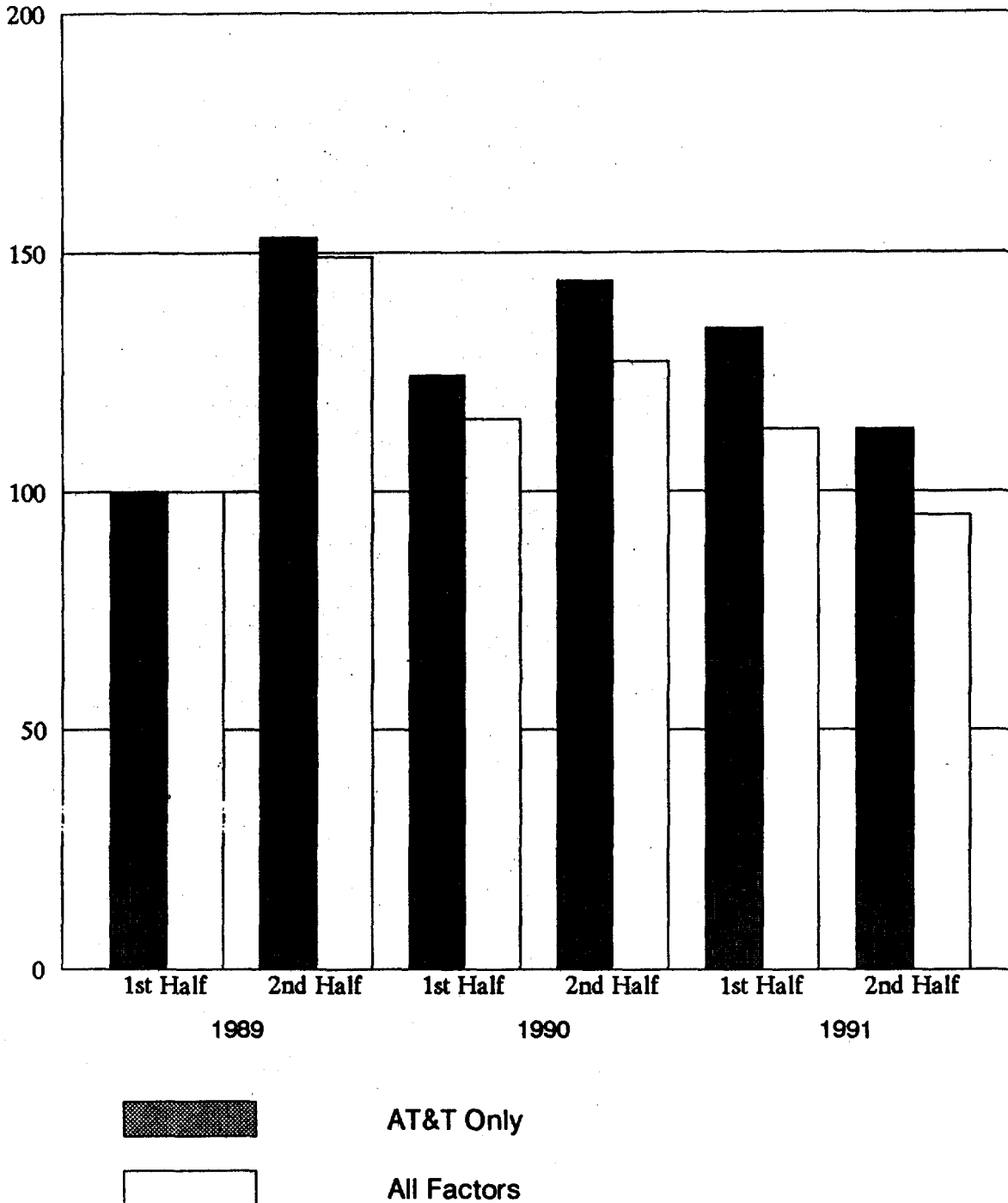
* Estimate.

Chart 6

AT&T's Equipment Blockage and Failure Index

(1989-1991)

Index, 1st Half 1989 = 100



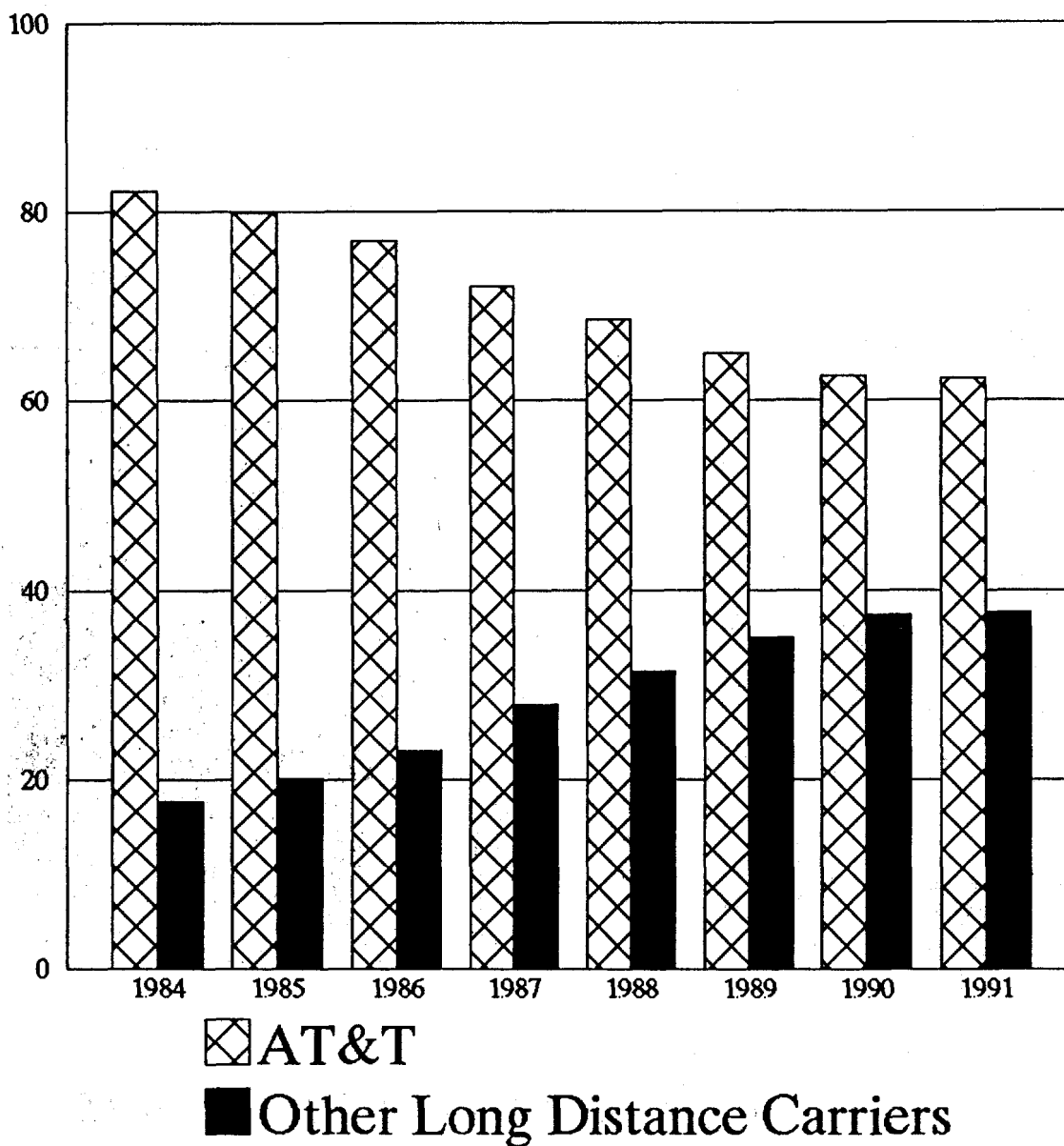
Source: FCC, Common Carrier Bureau, Industry Analysis Division.

Chart 7

AT&T's Market Share Interstate Switched Minutes of Use

(1984 - 1991)*

Percent Share



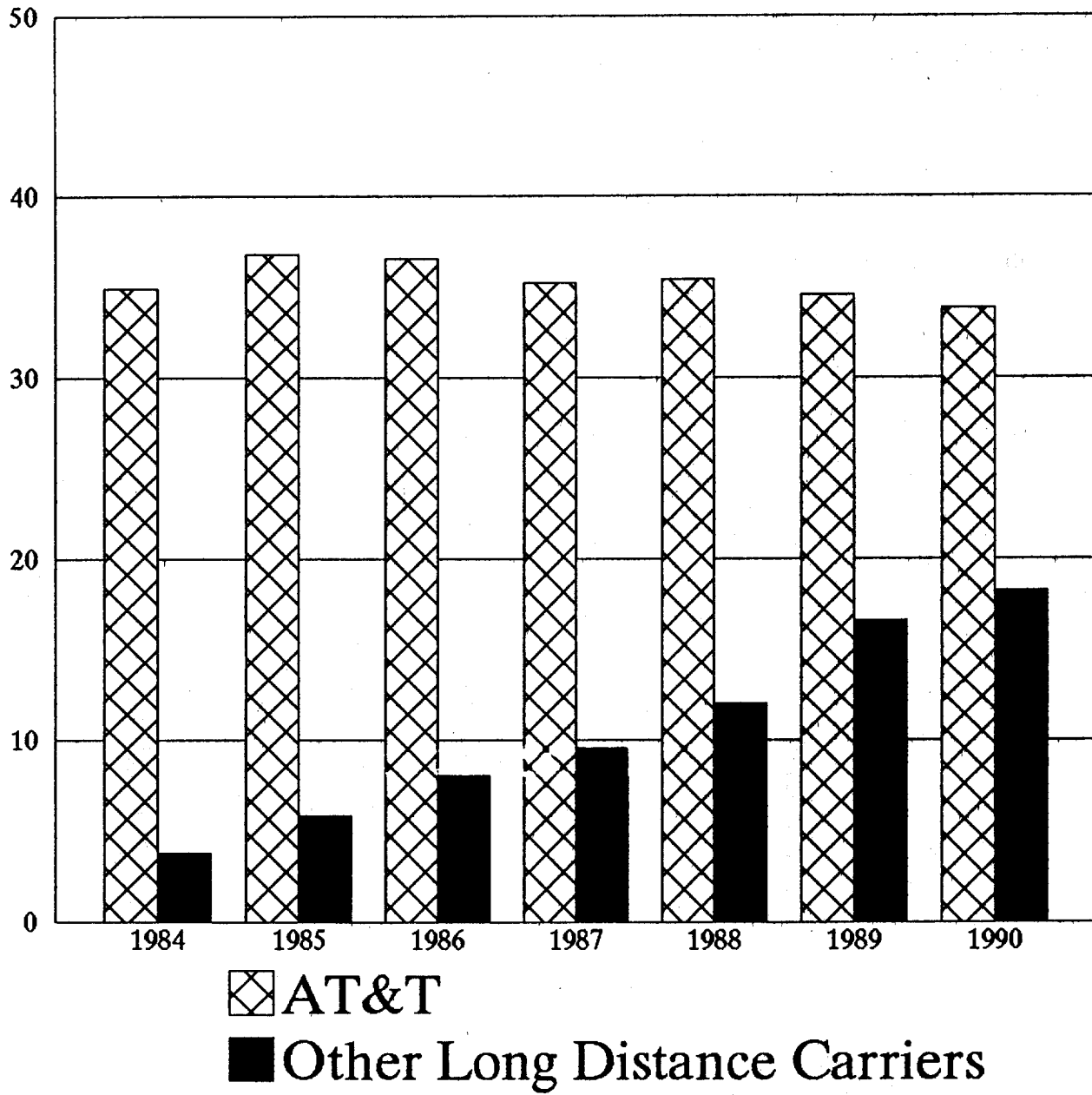
Source: FCC, Common Carrier Bureau, Industry Analysis Division. Long Distance Market Shares, 4th Quarter 1991, Released 3/24/92.

*Data for 1984 is based on the second half of the year. Data for first half 1984 was not available.

Chart 8

AT&T's Toll Revenues * Compared with Other Long Distance Carriers (1984-1990)

Billions of Dollars



Source: FCC, Common Carrier Bureau, Industry Analysis Division.

* Includes intrastate and interstate revenues.

Chart 9

Number of Long Distance Telephone Carriers

Year	End of Quarter	Using Equal Access		Total All Carriers	
		Common Carriers *	Total **	Common Carriers *	Total **
1986	1	--	169	--	--
	2	--	183	--	--
	3	--	190	--	506
	4	--	210	--	533
1987	1	--	211	--	561
	2	--	213	--	n/a
	3	--	224	--	n/a
	4	--	239	--	540
1988	1	--	238	--	511
	2	--	248	--	519
	3	--	256	--	506
	4	--	266	--	510
1989	1	--	274	--	519
	2	--	287	--	n/a
	3	--	304	--	n/a
	4	--	318	--	519
1990	1	289	295	466	512
	2	288	294	460	506
	3	304	311	462	511
	4	304	311	448	499
1991	1	306	314	446	505
	2	327	342	441	542
	3	337	352	455	528
	4	351	366	472	576

Source: FCC, Common Carrier Bureau, Industry Analysis Division. Summary of Long Distance Carriers, released March 17, 1992.

n/a: Data is not available.

* Separate data for common carriers was not available until 1990.

** Data includes firms not involved in common carriage.